Supreme Court, U. S.
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IN THE

Supreme Court of the United States

October Term, 1978

No. 79-490

PENNSYLVANIA BANK AND TRUST COMPANY,
Executor of the Estate of ETHEL S. BRICE,
Deceased, Petitioner

v.

UNITED STATES OF AMERICA

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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Executor of the Estate of ETHEL S. BRICE,
Deceased, Petitioner

v.

UNITED STATES OF AMERICA

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The petitioner Pennsylvania Bank and Trust Company respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Third Circuit entered in this proceeding on April 25, 1979.

OPINION BELOW

The opinion of the Court of Appeals which appears in the Appendix hereto has not yet been reported. The opinion of the District Court for the Western District of Pennsylvania is reported at 451 F. Supp. 1296.

JURISDICTION

The judgment of the United States Court of Appeals for the Third Circuit was entered on April 25, 1979, and pursuant to Mr. Justice Brennan's Order of

July 13, 1979 this petition for a writ of certiorari was filed within 150 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

QUESTION PRESENTED

Whether, for federal estate tax purposes, the estate of a deceased incompetent includes the value of a trust over which the decedent was at all material times legally incapable of exercising a general power of appointment.

STATUTORY PROVISIONS INVOLVED

Title 26 (Internal Revenue Code of 1954) Section 2041. Powers of Appointment.

(a) [as amended by Sec. 18(a) (2)(H), Revenue Act of 1962, P.L. 87-834, 76 Stat. 9601. In General.—The value of the gross estate shall include value of all property—

* * * *

(2) Powers created after October 21, 1942.—To the extent of any property with respect to which the decedent has at the time of his death a general power of appointment created after October 21, 1942, or with respect to which the decedent has at any time exercised or released such a power of appointment by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under sections 2035 to 2038, inclusive. For purposes of this paragraph (2), the power of appointment shall be considered to exist

on the date of the decedent's death even though the exercise of the power is subject to a precedent giving of notice or even though the exercise of the power takes effect only on the expiration of a stated period after its exercise, whether or not on or before the date of the decedent's death notice has been given or the power has been exercised.

* * * *

(b) Definitions.—For purposes of subsection (a)—

(1) General power of appointment.—The term "general power of appointment" means a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate;

STATEMENT OF THE CASE

Ethel S. Brice (hereinafter "decedent") was the beneficiary of a trust established for her by her husband, Dr. James W. Brice (hereinafter "Dr. Brice"), in a will executed on May 11, 1956. The value of this trust as reported in his estate for federal estate tax purposes was $717,391.08. Decedent was given the right to consume the entire principal of the trust during her life and to appoint by will to her estate, or in favor of named persons or classes of persons, the entire principal of the trust. In her will, dated September 11, 1959, decedent disclaimed any power of appointment, to which she might become entitled.

From and after April, 1960 decedent was at all times incompetent and lacked testamentary capacity. For the last seven years of her life (1962-1969) decedent never spoke nor appeared to understand anything said to her. She was completely disoriented and incoherent, unable to express any intelligent response to stimulation and incontinent of bowel and urine. Her condition was at all times progressive, hopeless and incurable. Until his death of February 9, 1965, Dr. Brice cared for decedent.

On February 12, 1965, three days after Dr. Brice's death, a petition to have the decedent declared incompetent was executed, and on March 31, 1965 the Orphans' Court of Crawford County, Pennsylvania duly found the decedent to be incompetent. Decedent died on August 15, 1969. It is undisputed that from a time prior to the grant of the power of appointment until she died, she continuously lacked the legal capacity to exercise the power and that under Pennsylvania law

the decedent's guardian was subject to an ascertainable standard with respect to how that power could be exercised.[1] Decedent's will dated September 11, 1959, was admitted to probate on August 22, 1969. On November 16, 1970, Petitioner, as Executor of the decedent's estate, filed a United States Estate Tax Return and paid federal estate tax of $483,430.51.

On November 14, 1973, Petitioner filed a claim for refund of federal estate tax in the amount of $347,427.30 plus interest. The claim for refund was based in part on the contention that the value of the trust created by Dr. Brice's will was not includable in the decedent's estate because at the time the trust was created and continuously thereafter she was incompetent and lacked testamentary capacity, so that she never had an exercisable power of appointment which would cause the trust property to be included in her estate under Section 2041(a) of the Internal Revenue Code. The claim for refund was disallowed with respect to this contention.

On February 2, 1976, the Petitioner filed this suit in the United States District Court for the Western District of Pennsylvania.[2] The District Court held that

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1. Since there is no dispute with respect to the standard imposed upon decedent's guardian the purported power to consume the principal of the trust during the decedent's life would not be considered a taxable general power of appointment.

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2. In addition to the issue noted above the complaint also sought a refund claiming (1) that a nuisance payment made to settle a will contest was deductible for federal estate tax purposes as an administrative expense (2) that certain United States Treasury Bonds (flower bonds) were improperly valued for federal estate

the value of the trust was includable in the decedent's estate notwithstanding the fact that she lacked the legal capacity to exercise the power of appointment from the time the power of appointment was created and at all material times thereafter. On April 25, 1979, the Court of Appeals affirmed this holding.

REASONS FOR GRANTING THE WRIT

The decision below conflicts with decisions of the United States Tax Court, the United States District Court for the Southern District of Florida and the United States District Court for the Western District of Texas, all of which are currently on appeal to the United States Court of Appeals for the Fifth Circuit.

Section 2041(a)(2) of the Internal Revenue Code of 1954 provides that there shall be included in a decedent's estate:

> any property with respect to which the decedent has at the time of his death a general power of appointment created after October 21, 1942.

Section 2041(b)(1) defines a general power of appointment as:

> a power which is *exercisable* in favor of the decedent, his estate, his creditors, or the creditors of his estate, (Emphasis supplied.)

---

tax purposes and (3) that the estate should be allowed a deduction for administration expenses for attorney's fees incurred in this tax controversy. The District Court did not find it necessary to reach a decision with respect to the last two issues and the Petitioner no longer asserts the contention raised in the first of these three issues.

Thus if a decedent, at the time of death possesses an "exercisable" power of appointment the property over which he possesses the power will be includable in his estate.

Neither the Internal Revenue Code nor the Regulations thereunder provide any guidance as to whether one lacking legal capacity can possess an "exercisable" power of appointment.[3]

As the Court of Appeals recognized, its holding was in conflict with that of *Finley v. United States,* 404 F. Supp. 200 (S.D. Fla., 1975) *appeal docketed,* C.A.5 No. 78-1066; *Estate of Gilchrist v. Commissioner,* 69 T.C.5 (1977), *appeal docketed,* C.A.5 No. 78-2400 and *Williams v. United States,* 78-2 U.S.T.C. par. 13,264 (W.D. Tex., 1978) *appeal docketed* C.A.5 No. 79-4116. The Court of Appeals stated, however, that *Finley* and *Gilchrist* were "wrongly decided" and would not be followed by it.

In *Finley,* as here, the decedent's husband's will created a trust over which the decedent was given a general power of appointment. Like the decedent here,

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3. On October 14, 1956, proposed Treasury Regulation 20.2041-3 was issued containing the following sentence:

> A power of appointment is considered to exist on the date of the decedent's death even though the decedent was at death and at all times since the creation of the power, under physical, mental or legal disability (whether or not adjudged incompetent).

When Final Treasury Regulation 20.2041-3(b) was issued on June 23, 1958 (T.D. No. 6296) the above quoted language was absent and no other language to that effect was ever substituted.

the decedent in *Finley* was incompetent, and from the time that the trust was created (*i.e.*, at her husband's death) "she lacked the legal capacity to exercise the general testamentary power of appointment of which she was donee." *Finley, supra,* p. 201.

Accordingly, the *Finley* court held that the assets subject to the general testamentary power of appointment were not includable in the gross estate of the decedent because she was incompetent and lacked testamentary capacity on and at all times after the date of the devise of the power (404 F. Supp. at 204):

> ... Margaret Whitlock from the time of devise of the general power of appointment until her death lacked the legal capacity to exercise the general testamentary power of appointment. This prevented her from possessing a general power of appointment within the meaning of Section 26 U.S.C. §2041(a)(2). Accordingly, the property forming the subject matter of the power should not have been includable in her gross estate for federal estate tax purposes.

In *Gilchrist v. Commissioner,* the Tax Court not only adopted the holding and rationale of *Finley,* it extended it. In *Gilchrist* the decedent's husband died on June 25, 1960, and in his will he bequeathed to his wife the "income, the use and benefits with full rights to sell or transfer all the remainder of [his] property, ... so long as she may live." Mrs. Gilchrist was also named executrix of the estate. She served as executrix from 1960 until she was adjudicated an incompetent on October 2, 1971. In *Gilchrist* the Tax Court stated that the issue was "whether Mrs. Gilchrist at the date of her death had a general power of appointment within the meaning of Section 2041(a)(2)...." The Tax Court held that the trust property was not includable in Mrs. Gilchrist's estate because under Texas law neither Mrs. Gilchrist nor her guardian possessed a taxable general power of appointment over the trust property at her death.

This same holding was also reached in *Williams v. United States.* There, the decedent's husband died in 1957 and in his will he left the decedent a life interest in his estate with a general power of appointment. On April 6, 1971, the decedent was adjudicated a person of unsound mind and she remained incompetent until her death on September 30, 1972. Between the time of her husband's death and her adjudication as an incompetent, the decedent never exercised her power of appointment.

The court in *Williams* followed the Tax Court's holding in *Gilchrist* and held that the property was not includable in decedent's estate because decedent:

> lost her general power of appointment upon her being adjudged incompetent, and having never exercised the power prior to that time, and the guardian under then existing Texas law being limited in her exercise of the power by "an ascertainable standard", it is clear that these circumstances fall within the exception to Section 2041 and are not properly taxable as part of the decedent's estate.

Thus, contrary to the holding of the Court of Appeals, it was held in *Finley, Gilchrist* and *Williams*, that property would not be included in a decedent's estate if at death he lacked the legal capacity to exercise a

general power of appointment over that property. To be sure in ***Estate of Alperstein v. Commissioner,*** 71 T.C. No. 32 (1978), *appeal docketed* C.A.2 No. 79-4116, the Tax Court held that property subject to a power of appointment would be included in a decedent's estate even though she was incompetent from the time the power was created until the time of her death. In so holding the Tax Court in *Alperstein* stated that an exercisable power of appointment refers to the *existence* of the power of the decedent to appoint rather than to his *capacity* to exercise that power. The Tax Court cited no authority for this proposition, nor did it set forth the reasoning by which it reached this conclusion. Moreover, this statement was contrary to the reasoning set forth by the Tax Court in *Gilchrist*. The Tax Court in *Alperstein* attempted to distinguish *Gilchrist* and *Finley* by noting that unlike the decedents in those cases, and unlike the decedent here, the decedent in *Alperstein* could have exercised the power "during a lucid interval."

Notwithstanding the decision in *Alperstein,* the Tax Court subsequently in ***Estate of Reid v. Commissioner,*** 71 T.C. No. 74 reaffirmed the reasoning and holding of *Gilchrist*. Specifically, in *Reid* the decedent established an inter vivos, irrevocable trust in 1955 and transferred property to a bank which served as trustee of the trust and had the discretionary right to distribute trust property and income therefrom to the designated beneficiaries of the trust during the life of the decedent. Additionally, the trust instrument provided that, in the event the trustee resigned, the decedent had the right to appoint a successor trustee. No provision in the trust instrument prohibited the decedent from appointing herself as a successor trustee so that she could have

had the *power* to direct the income of the trust. On January 21, 1972 the decedent was adjudicated an incompetent and her husband was appointed as guardian of her estate.

The Commissioner sought to include in the decedent's estate, under Section 2036(a) of the Internal Revenue Code[4] the fair market value of assets held by the trust. It was undisputed that had the decedent retained her competency the value of the assets in the trust would have been included in her estate. Nevertheless, the Tax Court in *Reid* followed its previous opinion in *Gilchrist* and held that because the decedent was adjudicated incompetent she was legally deprived of the power that she may otherwise have had to appoint herself as successor trustee and to designate who could receive income from the trust. Thus, the trust property was not includable in her estate. Specifically, the Tax Court in *Reid* noted that because the decedent in *Gilchrist* was legally incompetent she could not possess a general power of appointment at the time of her death. The Tax Court in *Reid* stated:

> Under the rationale of *Estate of Gilchrist* and the application of Texas law neither the decedent [in *Reid*] nor her guardian possessed ***the right to exercise the power to appoint*** a successor trustee . . . Once decedent was adjudicated incompetent she

4. Section 2036 of the Code causes property to be included in a decedent's estate if the property is transferred and the transferor retains (1) the possession or enjoyment of or the right to income from property or (2) the right either alone or in conjunction with another person to designate the persons who shall possess or enjoy the property or the income therefrom.

> was deprived of any right she may have held prior thereto. *Estate of Gilchrist* . . . (Emphasis supplied.)

Thus, in *Reid* the Tax Court reaffirmed its holding in *Gilchrist* that assets subject to a testamentary general power of appointment are not includable in the estate of a decedent for federal estate tax purposes if at death the decedent lacks the legal capacity to exercise the power.

Accordingly, the opinion of the Court of Appeals is in conflict with the opinions in *Finley, Williams* and *Gilchrist* and with the rationale of *Reid.* Furthermore, it must be noted that even if the Court of Appeals for the Fifth Circuit were to reverse the Tax Court's decision in *Gilchrist,* the Tax Court will continue, in other cases, to reach the same result as it did in *Gilchrist* unless such cases are appealable to the Third or Fifth Circuits. See *Golsen v. Commissioner,* 54 T.C. 742 (1970).

Unlike the holding of the Court of Appeals here, the result reached by the District Courts in *Finley* and *Williams* and by the Tax Court in *Gilchrist* was bottomed on the premise that in those cases the decedent lacked the *legal capacity* to exercise a general testamentary power of appointment. This rationale is in keeping with this Court's opinion in *Commissioner v. Noel Estate,* 380 U.S. 678. In *Noel* the question presented was whether a decedent who purchased life insurance policies shortly before boarding a fatal airplane flight possessed at his death any of the "incidents of ownership" in the policies so as to cause those policies to be included in his estate by virtue of Section 2041

(a) (2) of the Code. The decedent's estate argued that the policies were not includable in his estate because as a *practical* matter he would not have had the opportunity to exercise such incidents of ownership between the time that he purchased the policies and the crash of the plane. This Court held the proceeds of the policies were includable in the decedent's estate because estate tax liability depends on a "general *legal* power to exercise ownership, without regard to the owner's ability to exercise it at a particular moment."

The analysis of the Court of Appeals for the Fifth Circuit in *Estate of Bagley v. United States,* 443 F.2d 1266 was similar to that of this Court in *Noel.* In *Bagley* a husband and wife were killed in an automobile accident in which it could not be determined which spouse survived the other. The husband's will provided for the creation of a testamentary trust for the benefit of the wife during her lifetime and with a general testamentary power of appointment. The Fifth Circuit found the trust includable in the wife's estate because, under Florida law, during the theoretical instant that the wife survived her husband she had the *legal capacity* to exercise the power of appointment over the trust. It is important to note that in reaching its decision in *Bagley,* the Court of Appeals for the Fifth Circuit was careful to distinguish its earlier decision in *Jenkins v. United States,* 428 F.2d 538, (C.A.5, 1970) in which the question presented was whether a decedent had an *exercisable* power of appointment under Georgia law when the power was created in a will that was not probated during the lifetime of the decedent-donee. Although the Fifth Circuit found that there existed a general power of appointment in *Jenkins,* that result was reached only

after the Fifth Circuit interpreted Georgia law to determine whether the decedent possessed an exercisable power of appointment.

In reaching its holding, the Court of Appeals here unlike the *Noel, Bagley, Finley* and *Gilchrist* courts failed to consider the distinction between the lack of the legal capacity to possess a power of appointment and practical circumstances which might prevent the exercise of such a power. Rather, the Court of Appeals merely interpreted the term "exercisable" as used in Section 2041 to refer to the scope of the power set forth in the granting instrument, not to the donee's actual *legal* capacity to exercise it. The effect of this holding is to provide that a power of appointment is exercisable within the meaning of Section 2041 if *by its terms* it constitutes a general power of appointment. Yet, Section 2041 does not define a general power of appointment as one that appears to be exercisable by its terms. Rather, it defines a general power of appointment as one which is *exercisable* in favor of certain individuals or entities.

Finally, it must be noted that the result reached by the District Court in this case was ultimately bottomed on the assumption that to not impose taxation here would be contrary to the scheme of estate taxation.[5] Specifically, it relied upon what it believed would be the discontinuities that would arise between Section 2041 and the marital deduction provision of the Internal Revenue Code (currently Section 2056). This provision as enacted, and applicable at the time of the death of decedent and her husband, permitted a decedent to transfer to his surviving spouse upon his death up to one-half of his adjusted gross estate free of estate taxation. Such a transfer qualifies for the marital deduction if the interest left to the surviving spouse, in addition to meeting other requirements, is a "deductible interest"—an interest which will be taxable to the surviving spouse's estate at death. Oftentimes such an interest will be in the form of a life estate coupled with a general power of appointment. Section 2056(b)(5) of the Internal Revenue Code. Thus in a situation such as that presented here property might escape taxation in the estate of one spouse by virtue of the marital deduction and also escape taxation in the estate of the surviving spouse by virtue of her incompetency if she is given a life estate with a general power of appointment. The District Court in this case believed that such a result was not intended by Congress when it enacted the marital deduction provision of the Internal Revenue Code.

Notwithstanding the belief of the District Court with respect to the intent of Congress the result feared by the District Court would spring from the express language of Section 2041.[6] Moreover, it must be recognized that Congress enacted the marital deduction provision of the Internal Revenue Code several years *after* it provided for the estate taxation of powers of appointment. The subsequently enacted marital deduction pro-

5. The Court of Appeals did not direct itself to this question. Nevertheless, it "adopted as [its] own" the District Court's opinion "adding for completeness" its own "comments."

6. Perhaps in such a situation a marital deduction should not be allowed in the estate of the first spouse to die.

vision should not be used as an aid in the interpretation of Section 2041 since it is the legislative intent at the time of enactment and not Congress' afterthought which should be controlling. *Penn Mut. Life Ins. Co. v. Tedesco,* 252 U.S. 523.

Furthermore, it must be recognized that Section 2041's provisions are broader than the marital deduction provisions. All property over which a decedent possesses an exercisable power of appointment is includable in an estate regardless whether that property was the subject of a marital deduction or was left to someone other than a surviving spouse. Thus, the interpretation of the term exercisable as used in Section 2041 should not be governed by an asserted interrelationship between the marital deduction provision of the Internal Revenue Code and Section 2041. Rather, Section 2041, which is applicable in many situations not involving spouses must be read on its own.

CONCLUSION

The holding of the Court of Appeals conflicts with the holdings in *Finley, Gilchrist* and *Williams,* all of which are currently on appeal. We submit that these conflicts justify the grant of certiorari to review the judgment and opinion of the Third Circuit. In the event, however, that it is determined that these conflicts do not justify the grant of certiorari at this time, it is respectfully submitted that the ultimate determination of whether certiorari should be granted should only be made by this Court after the Court of Appeals for the Fifth Circuit has issued an opinion in *Finley, Gilchrist* or *Williams,* for if the holding of any of those cases is affirmed by the Court of Appeals for the Fifth Circuit, a conflict between the Courts of Appeals will exist.

Respectfully submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 78-1942

PENNSYLVANIA BANK AND TRUST COMPANY, Executor of the ESTATE OF ETHEL S. BRICE, DECEASED,

Plaintiff-Appellant

v.

UNITED STATES OF AMERICA,

Defendant-Appellee

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA

Argued February 23, 1979

Before: HUNTER and WEIS, *Circuit Judges* and MARKEY, *Chief Judge* of the United States Court of Customs and Patent Appeals.*

(Opinion filed April 25, 1979)

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Opinion of the Court

MARKEY, Chief Judge.

Refund action by Pennsylvania Bank and Trust Co. (Bank), executor of Ethel S. Brice (Brice), to recover federal estate taxes. The district court held a power of appointment given to Brice was part of the estate, though Brice was at all times incompetent to exercise the power. We affirm.

FACTS

Brice was the donee of a general power of appointment over a trust established by her husband's will. From a time prior to the grant of the power until she died, she lacked legal capacity to exercise that power. Brice's will stated an intention not to exercise the power. Brice's heirs contested her will, and the Bank settled by paying a total of $75,000 to five will contestants.

The Bank seeks to exclude from Brice's gross estate the value of the trust, to deduct the settlement amount, and to recover a resulting refund.

ISSUES

The dispositive issues are (1) whether Brice's estate, for federal estate tax purposes, includes the value of the trust when she was at all material times legally incompetent to exercise the power of appointment, and (2) whether the payment made in settlement was a deductible administration expense.

OPINION

Having considered the entire record, and heard oral argument, we agree with the judgment and well-

reasoned opinion of Judge Marsh, reported at 451 F. Supp. 1296. Seeing no value in recasting that opinion in words of our selection, we adopt as our own its relevant portions, adding for completeness these comments.

(1) *Power of Appointment*

Whether the cases relied on by the Bank, *Finley v. United States,* 404 F. Supp. 200 (S.D. Fla. 1975), *appeal docketed,* No. 78-1066 (5th Cir. Jan. 3, 1978) and *Estate of Gilchrist v. Commissioner,* 69 T.C. 5 (1977), *appeal docketed,* No. 78-2400 (5th Cir. June 20, 1978),* are significantly distinguishable on their facts, they are without binding effect here. Moreover, they were in our view wrongly decided and should not be followed in this circuit.

The Bank's attacks on the cases referred to by the district court are without merit. That the donee in *Fish v. United States,* 432 F.2d 1278 (9th Cir. 1970) was competent for a period prior to death is irrelevant. I.R.C. §2041(a)(2) makes the instant of death the critical time for ascertaining possession of a taxable power of appointment. In *Round v. Commissioner,* 332 F.2d 590 (1st Cir. 1964), the trust instrument termi-

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*The tax court follows the court to which appeal lies. *Golsen v. Commissioner,* 54 T.C. 742 (1970). *Estate of Reid v. Commissioner,* 71 T.C. No. 74 (Feb. 15, 1979), relied on by the Bank, is, like *Finley, supra,* and *Gilchrist, supra,* appealable to the Court of Appeals for the Fifth Circuit. In *Estate of Alperstein v. Commissioner,* 71 T.C. No. 32 (Dec. 6, 1978), from which appeal lies to the Court of Appeals for the Second Circuit, the existence of a power is held independent of the donee's capacity to exercise it.

nated decedent's power upon his permanent incapacity, unlike the present instrument granting Brice an unrestricted power. Although the inability of the decedent in *Commissioner v. Estate of Noel,* 380 U.S. 678 (1965), was due to particular circumstances other than an absence of legal capacity, that distinction provides no basis for reversal here.

In essence, the Bank's case founders on the shoals of the district court's statutory interpretation, with which we concur, i.e., that "exercisable" in I.R.C. §2041 refers to the scope of the power set forth in the granting instrument, not to the donee's actual capacity to exercise it.

The Bank's reliance on authorities not cited below is misplaced. *Estate of Minot v. Commissioner,* 45 T.C. 578 (1966) concerned a power created prior to October 21, 1942, and governed by I.R.C. §2041(a)(1), unlike the present power, governed by I.R.C. §2041(a)(2) and included in the gross estate whether or not exercised. *Estate of Stockdick v. Phinney,* 16 A.F.T.R.2d 6202 (S.D. Tex. June 14, 1965), holding that an incompetent surviving spouse cannot possess an "exercisable" power to qualify the interest for the marital deduction, is at odds with Treasury rulings consistently holding the mental capacity of a surviving spouse irrelevant. Rev. Rul. 75-350, 1975-2 C.B. 367; Rev. Rul. 55-518, 1955-2 C.B. 384. Moreover, in the authority relied on for the holding in *Stockdick, Starrett v. Commissioner,* 223 F.2d 163 (1st Cir. 1955), the trust instrument provided that the donee would lose certain rights upon becoming incompetent.

Final Treasury Regulation §20.2041-3(b) (1958) omitted this sentence from the October 1956 proposed regulation:

> A power of appointment is considered to exist on the date of the decedent's death even though the decedent was at death and at all times since the creation of the power, under physical, mental or legal disability (whether or not adjudged incompetent).

The Bank says the omission reflected Treasury's determination that the sentence was contrary to congressional intent. However, the Internal Revenue Service memo relied on by the Bank expressly says the sentence was "consistent with a published Revenue ruling [Rev. Rul. 55-518, *supra*]." Treasury's proposed regulations encompassed gift and estate taxes. Its proposal respecting gift taxes made competency relevant. The omitted sentence would have inconsistently made competency irrelevant with respect to estate taxes. Though present Treasury regulations respecting estate taxes are silent on the question of competency, the "inconsistency" has been resolved against the Bank's position. Treasury's gift tax regulation, §25.2503-4, promulgated November 15, 1958, and applicable to gifts made during 1955 and subsequent years, T.D. 6334, 23 Fed. Reg. 8904 (1958), provides that if a "minor is given a power of appointment * * * the fact that under the local law a minor is under a disability to exercise" the power "does not cause the transfer to fail to satisfy the conditions of section 2503(c)."

(2) *Administration Expense*

The Bank says the settlement payment is deductible because it preserved the estate against higher costs of

a "nuisance" suit and constituted only 4% of the estate. But the statutes and regulations permit deduction for claims based on personal obligations of the decedent, I.R.C. §2053; Treas. Reg. §20.2053-4 (1958), not for payment to an heir claiming as such. The status of the claimant is the determinative factor, not whether the claim is meritorious or whether the amount paid be a large or small percentage of the estate. Employment of the latter considerations as tests of deductability would be administratively unworkable.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit

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UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 78-1942

PENNSYLVANIA BANK AND TRUST COMPANY, Executor of the Estate of ETHEL S. BRICE, Deceased,

Appellant

v.

UNITED STATES OF AMERICA

(D. C. Civil No. 76-0155)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA

Present: HUNTER and WEIS, *Circuit Judges* and MARKEY, *Chief Judge of the United States Court of Customs and Patent Appeals**

Judgment

This cause came on to be heard on the record from the United States District Court for the Western District of Pennsylvania and was argued by counsel on February 23, 1979.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court, filed May 9, 1978, be, and the same is hereby affirmed. Costs taxed against appellant.

Attest:
BETTY J. ROBINSON
Deputy Clerk

April 25, 1979

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* Sitting by designation.

Appendix A.

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1978

No. .....

PENNSYLVANIA BANK AND TRUST COMPANY,
Executor of the Estate of ETHEL S. BRICE,
Deceased, Petitioner

v.

UNITED STATES OF AMERICA

I hereby certify that on this ..... day of September, 1979, three copies of the Petition for Writ of Certiorari were mailed, postage prepaid, to The Honorable Wade H. McCree, Jr., Esquire, Solicitor General, Room 5143 Main Justice Building, Tenth and Constitution Avenue, N.W., Washington, D. C. 20530. I further certify that all parties required to be served have been served.

CHARLES WEISS, Esq.

THORP, REED & ARMSTRONG
2900 Grant Building
Pittsburgh, PA 15219
288-7709

Supreme Court, U. S.
FILED
NOV 9 1979
MICHAEL RODAK, JR., CLERK

No. 79-490

In the Supreme Court of the United States

OCTOBER TERM, 1979

PENNSYLVANIA BANK AND TRUST COMPANY, ETC.,
PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

WADE H. McCREE, JR.
Solicitor General
Department of Justice
Washington, D.C. 20530

In the Supreme Court of the United States

OCTOBER TERM, 1979

No. 79-490

PENNSYLVANIA BANK AND TRUST COMPANY, ETC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

The sole question presented in this federal estate tax case is whether the decision below correctly held that the decedent's gross estate included the value of property over which she possessed a general power of appointment, as defined in Section 2041 of the Internal Revenue Code of 1954 (26 U.S.C.), even though she was legally incompetent at all times during the existence of the power and thus unable to exercise it under local law.

The pertinent facts may be summarized as follows: Petitioner is the executor of the estate of the decedent Ethel Brice. The decedent died testate on August 15, 1969, four years after the death of her husband, James Brice (R. 136, 137).[1] In his will, the decedent's husband established

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[1] "R." refers to the record appendix filed in the court of appeals.

a trust for the benefit of the decedent under which she was given the right during her life to consume or appoint by will the entire principal of the trust (Pet. App. 2a; R. 136). Shortly after her husband's death, the decedent was declared mentally incompetent on March 31, 1965 (R. 136). At no time between February 9, 1965, the date of death of the decedent's husband, until her own death on August 15, 1969, did the decedent exercise the general power of appointment created under the will of her husband (Pet. App. 2a).

Petitioner included the trust property subject to the decedent's power of appointment (valued at $717,391.08) in the decedent's gross estate on the federal estate tax return. It paid the estate tax due as shown on the return, but subsequently filed a claim for a refund, asserting that the trust corpus was not includable in the decedent's gross estate.

After the Commissioner disallowed petitioner's claim for a refund, it instituted this refund suit in the United States District Court for the Western District of Pennsylvania (Pet. 5; R. 137). The district court upheld the Commissioner's determination that the decedent's gross estate included the value of the trust property subject to the power of appointment. It ruled that an "exercisable" power of appointment, as that term is used in Section 2041, refers to the existence of the power in the decedent's behalf, rather than to the decedent's actual ability to exercise the power of appointment under local law at the time of death. Because the decedent's power by its terms was exercisable in favor of herself, the district court concluded that she had a general power of appointment despite her inability to exercise the power under local law (R. 145). The court of appeals affirmed on the basis of the district court's opinion (Pet. App. 1a-6a).

1. The decision below correctly held that the decedent's gross estate included the value of the trust property over which she had a power of appointment. Section 2041(a)(2) of the Code provides that the gross estate shall include the value of all property with respect to which the decedent has at the time of his death a "general power of appointment" created after October 21, 1942, whether or not the power has been exercised by the decedent. Section 2041(b)(1) defines a general power of appointment as a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate. As defined by her husband's will, the decedent's power of appointment was exercisable in such a manner. Under terms of the statute, it is therefore a general power of appointment within the meaning of Section 2041(b)(1).

The decision below is in accord with *Fish* v. *United States*, 432 F.2d 1278 (9th Cir. 1970). There, the court held that the inclusion of property in a decedent's gross estate is determined by the nature of the power as defined in the instrument creating the power, not by the donee's legal capacity to exercise that power. See also *Alperstein* v. *Commissioner*, 71 T.C. 351 (1978), appeal pending, No. 79-4116 (2d Cir.). The focus of Section 2041(a)(2) is on the decedent's property at the time of his death. Thus, as the court in *Fish* correctly observed (432 F.2d at 1280 n.3), if estate tax liability turned on the mental capacity of the decedent at the time of his death, the capacity of every donee of a power of appointment would be called into question because many of these people suffer some mental debilitation prior to death.

The decision below is also consistent with the legislative history of Section 2041. In 1942, Congress specifically amended the predecessor of Section 2041, which taxed only exercised powers of appointment. The revised statute

requires the inclusion of property subject to a power of appointment whether or not the power was exercised by the decedent. See Section 403(a) of the Revenue Act of 1942, ch. 619, 56 Stat. 942.[2] Since Congress enacted special relief provisions for donees of pre-1942 powers who were under a legal disability at the time of the change in the law (Section 403(d)(2) of the Revenue Act of 194 (56 Stat. 944)), it is clear that it intended that a post-1942 power held by a donee subject to a legal disability would be included in the donee's gross estate. If Congress intended to provide an exception for donees subject to a legal disability, it could have easily done so in Section 2041(b)(1), which contains certain express exceptions to the definition of a general power of appointment.

Finally, the court's interpretation of the term "power of appointment" in Section 2041(a)(2) is consistent with Section 2056, which allows an estate tax marital deduction for a property interest passing from the decedent to his spouse consisting of a life estate coupled with a general power of appointment. Section 2056(b)(5) provides that property subject to a power of appointment in the surviving spouse is eligible for the marital deduction if the power is "exercisable by such spouse alone and in all events." The Internal Revenue Service has ruled (Rev. Rul. 75-350, 1975-2 Cum. Bull. 367) that the legal capacity of the surviving spouse to exercise the power is irrelevant in determining the availability of the marital deduction under Section 2056(b)(5). If the rule were otherwise, the Service has pointed out that it could never be determined whether the surviving spouse could exercise the power "alone and in all events." On the other hand, under petitioner's position, the estate of the first

[2]Amending Section 811(f) of the Internal Revenue Code of 1939 (26 U.S.C. (1952 ed.)).

spouse to die may receive a marital deduction with respect to property which is subsequently excluded from the estate of the remaining spouse because of his or her incompetency, so that the property would be taxed in neither estate—a result Congress carefully sought to avoid.[3] See S. Rep. No. 1013, Pt. 2, 80th Cong., 2d Sess. 16 (1948); *United States* v. *Stapf*, 375 U.S. 118, 128 (1963). The only reasonable solution is that adopted by the decision below and the Service's ruling, *viz.*, that the legal capacity of a person to exercise a power of appointment is irrelevant both for purposes of determining the marital deduction allowable to the donor's estate and for determining the gross estate of the donee.

2. Petitioner contends (Pet. 6-12) that the decision below creates a potential conflict with other courts of appeals because four lower courts have held that the existence of a power of appointment does not trigger inclusion of the property subject to the power in the absence of legal capacity of the donee.[4] But conflicting trial court decisions do not provide a basis for invoking the discretionary jurisdiction of this Court.

Petitioner alternatively requests (Pet. 17) that the Court defer its decision on the petition pending resolution of the cases on appeal. But petitioner's request would require an inordinate delay in the Court's disposition of the instant

[3]Indeed, the record shows (R. 144) that the estate of the decedent's husband claimed and was allowed a marital deduction for the value of the property interest passing to the decedent.

[4]*Finley* v. *United States*, 404 F. Supp. 200 (S.D. Fla. 1975), appeal pending, No. 78-1066 (5th Cir.); *Estate of Gilchrist* v. *Commissioner*, 69 T.C. 5 (1977), appeal pending, No. 78-2400 (5th Cir.); *Williams* v. *United States*, 78-2 U.S. Tax Cas. para. 13,264 (W.D. Tex. 1978); appeal pending, No. 78-3797 (5th Cir.); *Estate of Reid* v. *Commissioner*, 71 T.C. 816, appeal pending, No. 79-3005 (5th Cir.).

case. Only one of those cases has been scheduled for oral argument in the court of appeals, and that case presents a jurisdictional issue which may preclude the court from even reaching the substantive issue presented here.[5] In these circumstances, there is no justification for petitioner's request for delay in the consideration of the petition.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. McCREE, JR.
Solicitor General

NOVEMBER 1979

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[5] *Finley* v. *United States*, *supra*, has been set for oral argument by the Fifth Circuit on December 4, 1979. In that case, the taxpayer filed a petition in the Tax Court for a redetermination of the estate tax liability after the refund suit was instituted in the district court. The government has argued that the district court lost jurisdiction over the case in accordance with Section 7422(e) of the Code when the petition was filed in the Tax Court. Should the court of appeals accept the government's jurisdictional argument, it will not reach the issue raised in the instant petition.

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Supreme Court, U. S.
FILED
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v.

UNITED STATES OF AMERICA

PETITIONER'S REPLY MEMORANDUM

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PETITIONER'S REPLY MEMORANDUM

1. The Government's reliance on *Fish v. United States,* 432 F.2d 1278 (C.A. 9, 1970) to support the opinion of the court below is misplaced. It is undisputed that from a time prior to the grant of the power until her death Mrs. Brice, the decedent here, continuously lacked legal capacity to exercise the power of appointment. Thus Mrs. Brice had no opportunity to determine the devolution of property. Unlike Mrs. Brice, the decedent in *Fish* was competent at the time the power of appointment was created, and she remained so for two years. This is a critical distinction, since—unlike Mrs. Brice—the decedent in *Fish* had two years within which to exercise legally a power of appointment. In short, the decedent in *Fish* had ample opportunity in fact *and in law* to determine the devolution of property—the hallmark of estate taxation—*Chase National Bank v. United States,* 248 U.S. 327, 334, 335, 338 (1929); Mrs. Brice admittedly had no such opportunity.

2. The Government also attempts to rely on Section 403(d)(2) of the Revenue Act of 1942 (56 Stat. 944). That provision, however, bears no relationship to the interpretation of the term "exercisable" as that term is used in Section 2041(a)(2) of the Internal Revenue Code. Rather, Section 403(d)(2) was merely a relief provision intended to aid those who were *temporarily* legally disabled, such as those serving in the military,[1] and who thus could not release or partially release powers of appointment at the time the law was changed in 1942 with respect to powers of appointment. See Paul, *Federal Estate and Gift Taxation,* 1946 Supplement p. 300. This relief provision, directed at those *temporarily* disabled from releasing a power, does not purport to define the term "exercisable" as used in Section 2041(a)(2), nor does it indicate a Congressional intent that a power of appointment be considered taxable and *"exercisable"* with respect to a donee—decedent who never had legal capacity to exercise the power. In order to accept the Government's interpretation of §403(d)(2) one would have to conclude that Congress intended to tax property which was never of any benefit to the decedent—donee and which she could never control. Any such conclusion would be contrary to the Congressional scheme of estate taxation designed to tax the use or control of property.

3. Finally, the Government tacitly recognizes that the decision of the court below is in conflict with four separate decisions of three courts, including the United

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1. Section 403(d)(2) provided in part that "an individual in the military or naval forces of the United States shall, until the termination of the present war be considered under a legal disability to release a power to appoint."

States Tax Court:

1. *Finley v. United States,* 404 F. Supp 200 (S.D. Fla. 1975), appeal pending, No. 78-1066 (5th Cir.);

2. *Estate of Gilchrist v. Commissioner,* 69 T.C. 5 (1977), appeal pending, No. 78-2400 (5th Cir.);

3. *Williams v. United States,* 78-2 U.S. Tax Cas. para 13,264 (W.D. Tex. 1978), appeal pending No. 78-3797 (5th Cir.);

4. *Estate of Reid v. Commissioner,* 71 T.C. 816, appeal pending, No. 79-3005 (5th Cir.).[2]

Nevertheless, the Government asserts that the conflict of the decision below with the decisions of the district courts and the Tax Court does not provide a basis for granting the petition and that if the Court were to defer its decision on the petition pending resolution of the cases on appeal there would result "an inordinate delay." This reference to "inordinate delay" betrays the weakness of the Government's position. As the Government notes, *Finley v. United States* has been set for oral argument by the Fifth Circuit on December 4, 1979—a few short weeks from the filing of this reply memorandum.[3] Accordingly, if this Court were to defer

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2. The Government does not dispute that even if the Court of Appeals for the Fifth Court were to reverse the Tax Court's decision in *Gilchrist* or *Reid,* the Tax Court will continue in other cases to reach the same result as in *Gilchrist* and *Reid* unless such cases are appealable to the Third or Fifth Circuits. See *Golsen v. Commissioner,* 54 T.C. 742 (1970).

3. It is only conjecture for the Government to suggest that *Finley* will be decided on jurisdictional grounds rather than on the merits.

its decision until *Finley* or the other cases were decided by the Fifth Circuit there would be no "inordinate delay". Moreover any assertion of "inordinate delay" is ill-founded because the petitioner seeks a *refund* of estate taxes that were paid in 1970. Thus only the petitioner and not the Government could be prejudiced by a delay in the disposition of this case.

In light of the conflicts between the decision below and the decisions of three other courts, including the United States Tax Court, it is respectfully submitted that certiorari be granted. In the alternative, if it is determined that the existing conflicts do not justify the grant of certiorari at this time, it is respectfully submitted that the ultimate determination as to the granting of certiorari be made after the Court of Appeals has issued an opinion in *Finley, Gilchrist* or *Williams.*

Respectfully submitted,

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